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INFO RUCPDO/DEPT OF COMMERCE WASHINGTON DC IMMEDIATE
RUEATRS/DEPT OF TREASURY WASHINGTON DC IMMEDIATE
RUCNASE/ASEAN MEMBER COLLECTIVE PRIORITY
RUEHBJ/AMEMBASSY BEIJING PRIORITY 3407
RUEHKO/AMEMBASSY TOKYO PRIORITY 8670
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STATE FOR EAP/MLS AND EB
TREASURY FOR OASIA
COMMERCE FOR EAP/MAC/OKSA
STATE PASS TO USTR FOR WEISEL
STATE PASS TO FEDERAL RESERVE SAN FRANCISCO FOR DAN FINEMAN
STATE PASS TO FEDERAL RESERVE NEW YORK FOR MATT HILDEBRANDT

E.O. 12958: N/A
TAGS: [EFIN](#) [ECON](#) [CH](#) [TH](#)
SUBJECT: THAI MARKETS UPDATE: CHINA CURRENCY POLICY AT
FAULT?

REF: BANGKOK 7504 AND PREVIOUS

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1. (SBU) While the Bank of Thailand has lifted the 30 percent reserve requirement on foreigners investing in Thai equities, the restriction remains in place for debt instruments. The President of the Thai Electronic Bond Exchange (a subsidiary of the Stock Exchange of Thailand) told the press that if the BoT policy regarding debt markets is not reversed "...the bond market will collapse." He continued, "The effect of the BoT policy is to make the bond market less active....and market sentiment is pushing up long-term yields." Kongkiat Opaswongkarn, CEO of Asia Plus Securities and President of the Thai capital Market Association, said that these views were "a bit extreme" but noted that the cost of capital in Thailand was certainly going to be higher than it was prior to December 19, although it was hard to say how much more expensive. A Standard and Poor's analyst has said that the new capital controls "will lead to higher funding costs in the Kingdom, with negative implications for the prices of debt and equity assets."

2. (SBU) With the RTG anticipated to run a budget deficit of Bt146 billion (US\$4 billion) for the coming fiscal year to be financed through the issuance of Treasury bills and bonds, the increased capital costs will directly affect the government budget going forward. For the private sector, increased risk premiums means that it will probably be more difficult to raise new equity, the cost of debt will be increased and liquidity in both markets reduced. These factors, plus the general malaise in the domestic economy, will pressure the BoT to reduce its policy rates at their January meeting. In the interim, f/x traders report the BoT is actively selling baht for US\$ and with the lower liquidity in domestic f/x markets, having some success in weakening the baht which was trading at around 36.1/US\$ around midday, from 35.7 yesterday evening.

3. (SBU) With the immediate crisis thought to be at bay, several market observers, including the BoT governor, have remarked both in the press and privately that the source of Thailand's strong baht situation is not just speculators

reportedly piling into the currency. They note that Thai monetary authorities have fewer tools at their disposal (or are more committed to relatively free currency markets) than other nations in the region including Taiwan, Japan and especially China. The Taiwan dollar and Yen have not significantly moved against the US\$ this year and the Yuan has appreciated only about 5.5 percent despite huge dollar inflows. With China the source of competition for many Thai exports and foreign direct investment, the Thais are most concerned at the slow rate of Yuan adjustment to US\$ weakness.

¶4. (SBU) BoT Governor Tarisa is quoted as saying that the problem of global trade and currency imbalances is widespread and "if this sort of problem is not cured in a cooperative manner...each country will have to find a way to take matters into its own hands." Exporters and capital market participants have separately told econoffs that the inflexibility of the Chinese currency is a major problem for both Thailand and the US. Kongkiat told us that he will encourage the RTG to work with ASEAN to press the Chinese government to allow the Yuan to appreciate more rapidly.

¶5. (SBU) Comment: Cynics may deride Governor Tarisa's comments as an attempt to deflect attention (criticism) from her own dubious management of the baht issue. There may be some of that, but an increasing number here agree with her basic complaint. While unwelcome, the current problems have the potentially salutary effect of focusing the RTG on what may be regarded as the root cause of the Kingdom's slow-motion decline in export competitiveness -- the rise of China. There is a consensus forming in Thailand that some of China's competitiveness is due not so much to any natural comparative advantage as to currency manipulation, and that Thailand can no longer afford to be passive or fatalistic on this point. We believe that Thailand, either by itself or in coordination with ASEAN, may be ready to work with the USG

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and others to press China for greater currency flexibility. As a first step, the US should consider extending an offer to the RTG's Finance Ministry and the Bank of Thailand to be briefed by their US counterparts on the recent US mission to China led by Treasury Secretary Paulson. Such a briefing could be combined with an exchange of views on how the US and Thailand could best cooperate in seeking progress on this issue.
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